

New York State Department of Taxation and Finance
Office of Tax Policy Analysis
Technical Services Division

TSB-A-09(2)C
Corporation Tax
March 2, 2009

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

PETITION NO. C080122B

On January 22, 2008, a Petition for Advisory Opinion was received from Service Lloyds Insurance Company, 6907 N. Capital of Texas Highway, Austin, Texas 78731. Petitioner, Service Lloyds Insurance Company, submitted additional information relating to the Petition on April 4, 2008.

The issue raised is whether Petitioner is subject to tax in New York State under Article 33 or Article 9-A of the Tax Law.

Petitioner submitted the following facts as the basis for this Advisory Opinion.

Petitioner is a non-life insurance corporation domiciled in the state of Texas that is not licensed to do an insurance business in the state of New York and has never generated any premiums allocable to New York since its incorporation on May 21, 1982.

Petitioner actively invests in a variety of investment vehicles such as stocks and bonds. In order to achieve higher returns, Petitioner sought the advice of an equity investor for more aggressive investments, such as limited partnerships. Accordingly, Petitioner made an initial investment of \$1.36 million in a limited partnership (LP) on July 26, 2006. Petitioner plans to make additional investments in LP in the future. Petitioner is a limited corporate partner whose investment is less than 1% of LP, and its only involvement in LP's activities is the investment of funds and receipt of quarterly and annual data on LP's operating results for financial and tax reporting purposes. Petitioner has no other authority to direct or control the operations of LP.

LP is an investment-driven partnership investing in underlying hedge fund managers, many of which operate in New York City. Most of the underlying hedge fund managers invest in stocks and bonds and generate passive income in the form of dividends, interest, and capital gains. However, some of the underlying hedge fund managers participate in lending and loan origination activities that generate both New York State and New York City income. This income is allocated to the funds and ultimately to the partners of these funds from the flow-through nature of the partnership investment.

LP is not a regulated investment company under section 851 of the Internal Revenue Code or a dealer in securities within the meaning of section 1236 of the Internal Revenue Code. LP derives more than 90% of its income from passive sources.

Applicable law and regulations

Section 209.4 of Article 9-A of the Tax Law provides, in part:

Corporations...taxable under articles thirty-two and thirty-three of this chapter...shall not be subject to tax under this article.

Section 1500 of Article 33 of the Tax Law contains general definitions and provides, in part:

(a) The term “insurance corporation” includes a corporation, association, joint stock company or association, person, society, aggregation or partnership, by whatever name known, doing an insurance business,...

* * *

(c) The term “foreign insurance corporation” means an insurance corporation incorporated or organized under the laws of any other state of the United States, the District of Columbia or the Commonwealth of Puerto Rico.

* * *

(e) The term “taxpayer” means any insurance corporation subject to the tax imposed under section fifteen hundred one, fifteen hundred two-a, or fifteen hundred ten or any captive insurance company subject to the tax imposed under section fifteen hundred two-b of this article.

Section 1501(a) of the Tax Law provides, in part:

Every domestic insurance corporation and every foreign or alien insurance corporation, for the privilege of exercising its corporate franchise, or of doing business, or of employing capital, or of owning or leasing property in this state in a corporate or organized capacity, or of maintaining an office in this state...shall annually pay a franchise tax which shall be computed as provided in section fifteen hundred two.

Section 1502 of the Tax Law provides, in part:

(a) The tax imposed under section fifteen hundred one shall be the greatest of:

- (1) for taxable years...beginning on or after January first, two thousand seven, seven and one-tenth percent of the taxpayer’s entire net income, or portion thereof allocated within this state, for the taxable year, or part thereof; or
- (2) one and six-tenths mills for each dollar of the taxpayer’s total business and investment capital allocated within this state for the taxable year, or part thereof... or
- (3) nine percent on thirty percent of the taxpayer’s entire net income plus salaries and other compensation paid to the taxpayer’s elected or appointed officers and

to every stockholder owning in excess of five percent of its issued capital stock minus fifteen thousand dollars and any net loss for the reported year, or the portion of such sum allocated within the state as hereinafter provided...or

(4) two hundred fifty dollars; plus

(b) eight-tenths of a mill for each dollar of the portion of the taxpayer's subsidiary capital allocated within the state for the taxable year,...

Section 1502-a of the Tax Law provides (for taxable years beginning on or after January 1, 2003):

In lieu of the tax imposed by section fifteen hundred one of this article, every domestic insurance corporation, every foreign insurance corporation and every alien insurance corporation, other than such corporations transacting the business of life insurance, (1) authorized to transact business in this state under a certificate of authority from the superintendent of insurance or (2) which is a risk retention group as defined in subsection (n) of section five thousand nine hundred two of the insurance law, shall, for the privilege of exercising corporate franchises or for carrying on business in a corporate or organized capacity within this state, and in addition to any other taxes imposed for such privilege, pay a tax on all gross direct premiums, less return premiums thereon, written on risks located or resident in this state. The tax imposed by this section shall be computed in the manner set forth in subdivision (a) of section fifteen hundred ten of this article as such subdivision applied to taxable years beginning before January first, two thousand three, except that the rate of tax imposed by this section shall be one and seventy-five hundredths percent on all gross direct premiums, less return premiums thereon, for accident and health insurance contracts, and two percent on all other such premiums. All the other provisions in section fifteen hundred ten of this article, other than subdivision (b) of such section, shall apply to the tax imposed by this section. In no event shall the tax imposed under this section be less than two hundred fifty dollars.

Section 1505(a)(1) of the Tax Law provides, in part:

Domestic, foreign and alien insurance corporations except life insurance corporations. Notwithstanding the provisions of section fifteen hundred one and fifteen hundred ten of this article, and except as otherwise provided in paragraph two of this subdivision, the amount of taxes imposed under such sections for taxable years beginning on or after January first, nineteen hundred seventy-seven and before January first, two thousand three, computed without regard to any credits...shall not exceed an amount computed as if such taxes were determined solely under section fifteen hundred ten, except that for purposes of the limitation provided herein, the rate of tax under such section shall be deemed to be...(iv) two percent for taxable years beginning after June thirtieth, two thousand two.

Section 1510(a) of the Tax Law provides, in part:

Domestic, foreign and alien insurance corporations except life insurance corporations. Except as hereinafter provided, for taxable years beginning before January first, two thousand three every domestic insurance corporation, every foreign insurance corporation and every alien insurance corporation, other than such corporations transacting the business of life insurance (1) authorized to transact business in this state under a certificate of authority from the superintendent of insurance or (2) which is a risk retention group as defined in subsection(n) of section five thousand nine hundred two of the insurance law, shall, for the privilege of exercising corporate franchises or for carrying on business in a corporate or organized capacity within this state, and in addition to any other taxes imposed for such privilege, pay a tax on all gross direct premiums, less return premiums thereon, written on risks located or resident in this state....

Section 1-3.2(a)(6) of the Business Corporation Franchise Tax Regulations (Regulations) provides, in part:

(i) A foreign corporation is doing business, employing capital, owning or leasing property or maintaining an office in New York State if it is a limited partner of a partnership, other than a portfolio investment partnership, which is doing business, employing capital, owning or leasing property or maintaining an office in New York State and if it is engaged, directly or indirectly, in the participation in or the domination or control of all or any portion of the business activities or affairs of the partnership. A foreign corporation is engaged in such manner in the business activities or affairs of the partnership if one or more of certain factual situations, including but not limited to the following, exist during the taxable year or, except for clause (a) of this subparagraph, any previous taxable year:

(a) The foreign corporation has a one percent or more interest as a limited partner in a partnership and/or the basis of the foreign corporation's interest in the limited partnership, determined pursuant to section 705 of the Internal Revenue Code, is more than \$1,000,000. For purposes of determining whether the level of interest in the partnership or level of basis of the interest in the partnership is met, the percentage of interest in the partnership and basis of interest in the partnership of members of the foreign corporation's affiliated group, of officers or directors of the foreign corporation or of officers or directors of members of the foreign corporation's affiliated group are added to the foreign corporation's interest in the partnership or the basis of its interest in the partnership, respectively.

* * *

(iii) As used in this paragraph, the following terms have these meanings:

* * *

(d) term *portfolio investment partnership* means a limited partnership which meets the gross income requirement of section 851(b)(2) of the Internal Revenue Code...The term *portfolio investment partnership* shall not include a dealer (within the meaning of section 1236 of the Internal Revenue Code) in stocks or securities.

Section 851(b)(2) of the Internal Revenue Code contains some of the requirements for a corporation to be considered a regulated investment company and provides:

at least 90 percent of its gross income is derived from-

- (A) dividends, interest, payments with respect to securities loans (as defined in section 512(a)(5)), and gains from the sale or other disposition of stock or securities (as defined in section 2(a)(36) of the Investment Company Act of 1940, as amended) or foreign currencies, or other income (including but not limited to gains from options, futures or forward contracts) derived with respect to its business of investing in such stock, securities, or currencies, and
- (B) net income derived from an interest in a qualified publicly traded partnership (as defined in subsection (h));

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Section 1501(a) of Article 33 of the Tax Law imposes a franchise tax on every foreign insurance corporation for the privilege of doing business, employing capital, owning or leasing property in New York State in a corporate or organized capacity, or maintaining an office in New York State.

The provisions in Article 33 of the Tax Law should be regarded as being *in pari materia* and construed in a like manner as substantially identical provisions contained in Article 9-A of the Tax Law. (*Royal Indemnity Co. v NYS Tax App Trib*, 75 NY2d 75; L1974, ch 649, §12) For purposes of Article 9-A of the Tax Law, section 1-3.2(a)(6) of the Regulations provides that a foreign corporation is doing business, employing capital, owning or leasing property, or maintaining an office in New York if it is a limited partner in a partnership, other than a portfolio investment partnership, that is doing business, employing capital, owning or leasing property, or maintaining an office in New York State and such foreign corporation is engaged directly or indirectly in the participation in or the domination and control of the partnership's business activities. A portfolio investment partnership is a limited partnership that meets the gross income requirement outlined in section 851(b)(2) of the Internal Revenue Code. Whether LP is a portfolio investment partnership as defined in section 1-3.2(a)(6)(iii) of the Regulations is a factual matter that cannot be determined in the scope of this Advisory Opinion. However, if LP is a portfolio investment partnership, Petitioner will not be deemed to be doing business in New York and will not be subject to tax solely by reason of its ownership in LP.

If it is determined that LP is not a portfolio investment partnership within the meaning of section 1-3.2(a)(6)(iii) of the Regulations, Petitioner's ownership interest in the partnership must be examined to determine whether Petitioner is engaged directly or indirectly in the participation in or the domination and control of the partnership's business activities. Section 1-3.2(a)(6)(i)(a) of the Regulations provides that a foreign corporation that owns a limited partnership interest of 1% or more or has an interest with a basis of more than \$1 million at any time during a taxable year is engaged in the participation in or the domination and control of the partnership's activities.

Petitioner is a limited corporate partner in LP, a partnership that is conducting business in New York State. Petitioner's ownership interest in LP is less than 1% of the partnership, and its only involvement in LP's activities is the investment of funds and receipt of quarterly and annual data on LP's operating results for financial and tax reporting purposes. However, Petitioner's basis in LP at the time of the initial investment in 2006 was \$1.36 million. Therefore, pursuant to section 1-3.2(a)(6) of the Regulations, Petitioner is deemed to be engaged in the participation in or domination and control of the partnership during 2006 and any subsequent tax year in which Petitioner's ownership interest or basis in the partnership meets either the ownership interest or basis threshold established in section 1-3.2(a)(6) of the Regulations.

In *Bankers Life and Casualty Company*, Adv Op Comm T & F, April 1, 2004, TSB-A-04(2)C, it was held that the petitioner was doing business, employing capital, owning or leasing property, or maintaining an office in New York through its ownership interests in partnerships and LLCs conducting business activities in New York. As in *Bankers Life, supra*, Petitioner will be deemed to be doing business, employing capital, owning or leasing property, or maintaining an office in New York State for purposes of Article 9-A through its ownership interest in LP, provided that LP is not a portfolio investment partnership. Activity that constitutes doing business, employing capital, owning or leasing property, or maintaining an office in New York for purposes of Article 9-A would also constitute such activities for section 1501 of the Tax Law. If LP is not a portfolio investment partnership, Petitioner is an insurance corporation that will be doing business, employing capital, owning or leasing property, or maintaining an office in New York State, and Petitioner, therefore, will be subject to tax under Article 33 of the Tax Law. See *Royal Indemnity, supra*.

Section 209.4 of Article 9-A of the Tax Law provides that a corporation that is taxable under Article 33 of the Tax Law is not subject to tax under Article 9-A of the Tax Law.

Section 1501 of the Tax Law provides that the tax due for an insurance corporation subject to tax under Article 33 will be computed pursuant to section 1502 of the Tax Law. Section 1502 provides that insurance corporations must pay the highest amount of tax computed on four bases: (1) a tax on allocated entire net income; (2) a tax on allocated business and investment capital; (3) a tax on a prescribed portion of entire net income plus salaries and other compensation of elected or appointed officers and certain stockholders; or (4) a fixed dollar minimum tax of \$250. However, section 1502-a imposes a tax on premiums in lieu of the taxes imposed under section 1501 (computed under the provisions of section 1502) on every foreign non-life insurance corporation that is authorized by the Superintendent of Insurance to transact business in New York or that is a

risk retention group. Petitioner is not authorized by the New York State Insurance Department to transact business in New York and is not a risk retention group. Therefore, the provisions of section 1502-a of the Tax Law do not apply.

Section 1505(a)(1) provides a limitation on the amount of tax paid by non-life insurance corporations for taxable years that began before January 1, 2003. Since Petitioner's inquiry is regarding a taxable year that begins after January 1, 2003, the limitation provided under section 1505(a)(1) does not apply.

Section 1510(a) imposes an additional tax based on premiums on non-life insurance corporations that (1) are authorized to transact business in this state under a certificate of authority issued by the Superintendent of Insurance or (2) are a risk retention group. This section of the Tax Law applies to taxable years that began before January 1, 2003. Therefore, the additional tax imposed under section 1510(a) does not apply.

Accordingly, provided that LP is not a portfolio investment partnership, Petitioner will be a taxpayer under section 1500(e) of Article 33 of the Tax Law, and pursuant to section 1515, will be required to file annual returns. Petitioner will be required to pay the tax on the highest of the four bases computed pursuant to section 1502. Petitioner's tax will not be limited pursuant to section 1505(a)(1), and Petitioner will not be required to pay the additional tax on premiums pursuant to section 1510(a).

DATED: March 2, 2009

/s/
Jonathan Pessen
Director of Advisory Opinions
Office of Counsel

NOTE: An Advisory Opinion is issued at the request of a person or entity. It is limited to the facts set forth therein and is binding on the Department only with respect to the person or entity to whom it is issued and only if the person or entity fully and accurately describes all relevant facts. An Advisory Opinion is based on the law, regulations, and Department policies in effect as of the date the Opinion is issued or for the specific time period at issue in the Opinion.